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SUBJECT: H1N1 ECONOMIC RELIEF PACKAGE - BEST MEDICINE?

11. (SBU) Summary: In an effort to resuscitate an economy laid low by the flu, on May 5 the Mexican government unveiled a stimulus package totaling 18.8 billion pesos (USD 1.4 billion). As the hardest hit sectors, tourism and SMEs will be the main beneficiaries of the plan, although Mexico's pork producers will also receive some assistance. Public reaction to the stimulus package has been mixed.

The government has been praised for its swift action and its responsiveness, but businesses and analysts assert that this aid package is insufficient. With Mexico already hit hard by a recession, the adjusted government 2009 GDP forecast now stands at -4.5 percent. The H1N1 outbreak has only made a recovery more difficult. End Summary.

THE PACKAGE

12. (U) On the final day of a five-day shutdown of commercial activity meant to slow the spread of the H1N1 virus, Finance Minister Carstens acknowledged in a press conference that the flu outbreak will have a "significant" impact on Mexico's economy. Based on his ministry's study of similar cataclysmic events in other countries, he said the impact could be between 0.3 and 0.5 percent of Mexico's GDP, which was USD 1.14 trillion in 2008. Unlike similar natural disasters however, Mexico's economic infrastructure remains intact and therefore, Carstens stressed, Mexico will likely recover quickly. Many analysts have countered that because of the current recession facing Mexico, the recovery could take a little longer. Indeed, the Mexican government's new GDP forecast for 2009, adjusted to include the maximum 0.5 percent impact of H1N1, now stands at negative 4.5 percent. Independent analysts believe the economy will shrink even further, by as much 5.9 percent.

13. (U) Carstens outlined seven economic supports to help Mexico recover quickly. First, the Finance Ministry assumes that given the maximum impact of 0.5 percent of Mexico's GDP, tax collection will fall by 10 billion pesos (USD 760 million). However, the Mexican government will make no attempt, such as implementing new taxes, to recoup these estimated losses. To foster liquidity, the government will allow businesses to deduct around 2 billion pesos (USD 150 million) in excess business flat tax (IETU) payments from their monthly payments of the ISR income tax. To protect employment, businesses will be granted a 20 percent reduction in employee health care payments in the IMSS social security system over the next two months (an estimated 2.2 billion pesos or USD 167 million).

SHORING UP TOURISM

14. (U) The package also proposes a reimbursement to the states for

businesses in the tourism sector of 25 percent of their losses over the next three months (an estimated 500 million pesos or USD 38 million). In effect, the government will compensate 25 percent of their tax collection losses to those states that authorize tax exemptions on the local 2 percent payroll tax and lodging taxes. To assist the airlines and cruise ships, there is a compensation package of about 250 million pesos - USD 19 million, consisting of a 50 percent reduction in air traffic control fees, but only for those few airlines that are not behind on their payments. The government also proposes halving the port docking fees for cruise ships and migration fees for the next three months. An additional 200 million pesos (USD 15.3 million) will be used to promote tourism in Mexico. Finally, 2.2 billion pesos (USD 167 million) in loans and loan guarantees will be made available to SMEs in the tourism industry, as well as to airlines and pork producers. Together, with the anticipated tax exemptions by state governments for lodging and payroll fees (1.4 billion pesos - USD 160 million), the total stimulus package amounts to 18.8 billion pesos (USD 1.4 billion).

BUSINESS REACTION IS LUKEWARM

15. (U) Many in Mexico's business sector have given the stimulus package mixed reviews. The president of Mexico City's National Chamber of Commerce (CANACO) told reporters that the government assistance was welcome, but he was not sure it was enough. "We hope that this is only the one of the first steps in economic aid," he said. Outside of Mexico City, Nuevo Leon business leaders were highly critical of the government's plan to reduce taxes to support businesses hurt by H1N1 flu closing, and called the measures absurd. They told the local press that the package was a farce, as the

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government was already unable to collect the taxes that were reduced in the relief plan. In Ciudad Juarez, many business leaders welcomed the assistance, but opined that the measures fall far short of meeting the needs of the business community. The government-mandated closures, they argue, resulted in millions of dollars in lost revenue which will not be fully recovered as a result of this relief package.

ANALYSTS SIMILARLY UNIMPRESSED

16. (SBU) AmCham Mexico's economist told EconOffs May 6 she suspected that the plan's impact would be "fairly insignificant." Since more than half of the plan's 18.8 billion pesos were actually simply tax reductions, the government's injection of funds into the economy was rather limited; i.e., only 8.8 billion pesos (USD 669 million) in relief, or a mere .07 percent of Mexico's GDP. (Note: By contrast, tourism generated \$13.3 billion in revenue in 2008, or 7 percent of GDP - Mexico's third largest source of foreign income. Tourism Secretary Rodolfo Elizondo has been quoted in the press as saying that losses in this sector could exceed 40 percent this year as frightened travelers stay away. End note.) She pointed out that the real difficulties remain the recession, declining production, and falling consumption.

17. Other analysts concur that this package is not enough, but given that Mexico faces an economic recession, a decline in oil revenues, and a shortfall in tax revenues, this is realistically the extent of what the government can offer. The Mexican Congress mandates a balanced book; Congress has already authorized a deficit of 1.8 percent of its GDP. Carstens and the Calderon Administration could appeal to Congress to authorize a deeper deficit, but experts do not believe anything above 2 percent as politically viable. The government's domestic debt - 21.5 percent of GDP - and its foreign debt - 5 percent - are still manageable, but would become less so if encumbered by additional obligations.

PORK PRODUCERS

18. (U) The National Organization of Pork Producers in Mexico stated that while the package would help offset some of the damage caused by H1N1, it alone is not enough. They estimate their losses at 2.5

billion pesos, above the 2.2 billion pesos in loans and loan guarantees (USD 167 million) to be extended to pork producers, SME's, and airlines. The pork producers encouraged the Agriculture Secretariat to grant an additional 100 million pesos (USD 7.6 million) in lines of credit.

STATES' RESPONSE

¶9. (U) For their part, Mexico's 32 states responded to the federal government's stimulus plan through a public request by the Association of Economic Development Secretaries. They called for: the expansion of the federal stimulus package; additional economic supports for SME's affected by the outbreak through a program of direct, timely and flexible credits; the acceleration of the government procurement program for Mexican SMEs, and; the implementation of an intensive overseas promotion campaign for Mexican products.

COMMENT

¶10. (SBU) Comment: Reaction to the stimulus package introduced by Minister Carstens has been mixed, with hard-hit businesses - particularly in the tourism sector - wanting more. The Mexican government appears to be extending as much assistance as it can. However, it may not be absorbing all the costs related to the outbreak. Responding to criticism, Carstens stated that should it become necessary, the government is leaving the door open for additional measures. However, it will not be easy for the government to release more funds during the first half of the year. Even using the most sophisticated model to compare this outbreak with similar events in other countries, it is still too early to know the full extent of the impact of H1N1 on the Mexican economy. The worst of the H1N1 epidemic may be over in Mexico, but the patient is still suffering from other complications. End Comment.

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BASSETT